17

Supreme Court, U.S.
FILED
MAY 4 1953
HAROLD B. WILLEY, Clerk

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 59

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA (FORMERLY ETERPEN, S. A.),
Petitioner,

vs.

THE UNITED STATES

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS AND BRIEF IN SUPPORT THEREOF.

WILLIAM A. PATTY,
Counsel for Petitioner,
20 Exchange Place,
New York 5, New York.

SHARON CLAY RISK,
Of Counsel.

INDEX

Subject Index

	Page
Petition	1
Opinion Below	2
Jurisdiction	2
Questions Presented	2
The Statutes and Regulations Involved	2
Summary Statement of Matters Involved	2
Reasons for Granting the Writ	5
I. The Decision of the Court Below is in Conflict With Numerous Decisions, including Decisions of this Court, the Courts of Appeals and the Tax Court	5
II. The Court Below Committed Palpable Error in Holding as a Matter of Law that the Exclusive License Agreement was not an Assignment of the Patents	6
III. This Case Raises an Important Question of Federal Income Tax Law which has not been, but should be, Settled by this Court	7
Specification of Errors to be Urged	8
Prayer	9
Brief	11
The Statutes and Regulations	11
Argument	13
I. An Exclusive License to Make, Use and Vend is a Sale	14
II. The Court Below Committed Palpable Error in Holding as a Matter of Law that the Exclusive License Agreement was not a Sale	18
First Major Error—the Purpose and Effect of the Option Agreement	18
The Exclusive License Effected a Sale on Installments Secured by a Purchase Money Mortgage	19

Page

Second Major Error—That the Licensees Could Not Sue for Infringement in Their Own Names . . . 21
Third Major Error—Disregard of Sworn Statement as to Intention of parties . . . 23
Unjustified Inference from the December 1, 1946 Agreement . . . 25
The Option Agreement Had Some Purpose Other Than an Alternative Purchase Price . . . 26
Reliance Upon Absence of a Provision for Application of Royalties Towards a Fixed Purchase Price . . . 27
Reliance on Absence of a Reason for Disregarding the Form of the Agreements . . . 28
Conclusion . . . 28

Table of Cases Cited

Cases:

Allen v. *Werner*, 190 F.2d 840 (5th Cir. 1951) . . . 5
Bloch v. *United States*, 200 F.2d 63 (2d Cir. 1952), cert. den. 345 U.S. 935 (1953) . . . 7, 18
Commissioner v. *Celanese Corporation of America*, 140 F.2d 339 (D.C.Cir. 1944) . . . 14
Commissioner v. *Wodehouse*, 337 U.S. 369, (1949) . . . 14
Dreymann v. *Commissioner*, 11 T.C. 153 (1948) . . . 5, 8, 18
Eterpen Financiera Sociedad De Responsabilidad Limitada, 108 F.Supp. 100 (1952) . . . 2
Federal Laboratories, Inc. v. *Commissioner*, 8 T.C. 1150 (1947) . . . 16
Green v. *Le Clair*, 24 F.2d 74 (7th Cir. 1928), 5, 8, 16, 19, 21
Hessert v. *Commissioner*, 6 T.C.M. 1190 (1947) . . . 26
Hofferbert v. *Briggs*, 178 F. 2d 743 (4th Cir. 1949) . . . 5, 18
Kavanagh v. *Evans*, 188 F.2d 234 (6th Cir. 1951) . . . 5, 8, 17, 18, 21

Page

Kimble Glass Co. v. *Commissioner*, 9 T.C. 182 (1947) 5, 8, 18
Kronner v. *United States*, 110 F. Supp. 730 (Ct. Cl. 1953) 21
Lamar v. *Granger*, 99 F. Supp. 17 (W.D. Pa., 1951) 27, 29
Littlefield v. *Perry*, 88 U.S. 205 (1874) 5, 8
Myers v. *Commissioner*, 6 T.C. 258 (1946) 5, 8, 18, 26
Parke, Davis & Co. v. *Commissioner*, 31 B.T.A. 427 (1934) 5, 8, 18
Pike v. *United States*, 101 F.Supp. 100 (D.Conn. 1951) 23, 27
Rhodes-Hochriem Mfg. Co. v. *International Ticket Scale Corp.*, 57 F.2d 713 (D. Del. 1932) 16
Taylor v. *Commissioner*, 16 T.C. 376 (1951) 5, 8, 18
Thompson v. *Johnson* (D.C. S.D.N.Y. 1950), 50-2 U.S.T.C. Par. 9428 26
United States v. *General Electric Co.*, 272 U.S. 476 (1926) 5, 8
Waterman v. *Mackenzie*, 138 U.S. 252 (1891), 5, 8, 14, 17, 21, 28, 30

STATUTES AND OTHER AUTHORITIES CITED

United States Code:

Title 28:

Section 1255(1) 2
Section 1651(a) 2
Section 2101(c) 2

Internal Revenue Code:

Section 119(a)(4) 13
Section 143(b) 12, 13
Section 144 12
Section 231(a)(1) 11

Treasury Regulations:

Regulations 111:

Section 29.143-2 13
Section 29.231-1(a) 12
Section 29.231-2(a) 12

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 59

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA (FORMERLY ETERPEN, S. A.),
Petitioner,

vs.

THE UNITED STATES

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner, Eterpen Financiera Sociedad de Responsabilidad Limitada, hereby respectfully requests this Honorable Court to issue a writ of certiorari to review the decision and judgment of the United States Court of Claims in the above-entitled case, entered on November 4, 1952, which denied petitioner's motion for summary judgment, granted respondent's cross-motion for summary judgment and dismissed the petition for refund of $115,822.21 in taxes claimed to have been wrongfully withheld, together with interest thereon.

Opinion Below

The opinion of the Court of Claims of the United States (R. 64-75) is reported in *Eterpen Financiera Sociedad de Responsabilidad Limitada* v. *United States*, 108 F. Supp. 100 (1952).

Jurisdiction

The judgment of the Court of Claims of the United States, sought to be reviewed, was entered on November 4, 1952 (R. 75). The petitioner seasonably filed a motion for rehearing on December 4, 1952 (R. 75). That motion was entertained and on February, 1953 denied (R. 76). The jurisdiction of this Court is invoked under Title 28, United States Code, Sections 1255 (1), 1651(a) and 2101(c).

Question Presented

Was petitioner, a foreign corporation not engaged in trade or business within the United States, subject to tax on certain payments received from domestic corporations on the ground that they represented mere royalties for the use of United States patents, as contended by the respondent, or were the payments exempt from tax as proceeds of the sale of the patents, as contended by the petitioner?

The Statutes and Regulations Involved

The pertinent statutory provisions and regulations are set forth in the accompanying brief, *infra*, pp. 11-13.

Summary Statement of Matters Involved

Petitioner, Eterpen Financiera Sociedad de Responsabilidad Limitada (herein sometimes called "Eterpen"), was and is an Argentine corporation not engaged in trade or business within the United States (R. 64). In 1945 Eterpen was the possessor of certain United States patents

and pending patent applications (hereinafter called the "patents"), on a ball-pointed fountain pen known as the "Biro Pen", and on a pulpy ink or writing paste for use therein (R. 8).

On May 18, 1945 Eterpen entered into a so-called "License Agreement" (R. 7-26) with two domestic corporations, Eversharp, Inc. and Eberhard Faber Corporation (hereinafter called "Eversharp" and "Eberhard"), whereby Eterpen granted and conveyed to those companies, jointly, the exclusive right and license under said patents to "make, use and vend" the protected pen and ink inventions throughout the United States, Hawaii and Alaska (herein sometimes referred to as the "Licensees' Area") during the full life of said patents (R. 9). In return, Eversharp and Eberhard agreed to pay to Eterpen royalties based upon the net sales price of all articles sold under said patents after deduction of certain costs and expenses (R. 15).

It was intended that the whole bundle of rights under the patents be transferred by the License Agreement to Eversharp and Eberhard (R. 48). The reason the transfer was made in the form of a license rather than an assignment was to protect Eterpen in the event of default on the payments for the patents (R. 48).

Simultaneously with the execution of the foregoing Agreement, the parties executed an agreement entitled "Option" (R. 33-39). Under the terms of this agreement Eterpen as "Optionor" and Eversharp and Eberhard as "Optionees" agreed that in consideration of the execution of the License Agreement (R. 33) the Optionor granted to the Optionees the option to pay a lump sum of $1,500,000 (R. 37) for the acquisition of the entire right, title and interest in the patents and in lieu of further installment payments (R. 49).

The Option by its terms expired on March 1, 1946 (R. 37-

38). Prior to March 1, 1946, no pens had been sold (R. 48). From March through September, 1946, Eversharp's sales were large and the royalties due Eterpen under the License Agreement amounted to $402,757.72 (R. 48-49). From July through December, 1946, Eberhard's sales were substantial, and the royalties due Eterpen amounted to $84,329.66 (R. 67). Because the Christmas Season was approaching and sales were expected to increase greatly during the last quarter of 1946, Eversharp commenced negotiations for a lump sum payment (R. 48-49). Eversharp refused to pay more than $1,050,000 on the ground that it and Eberhard had already paid more than $450,000 under the License Agreement (R. 49). It was finally agreed that Eversharp would be permitted to exercise the option by paying an additional $1,050,000, and a Memorandum of Agreement (R. 40-46) was executed as of December 1, 1946 (R. 45). The rights of Eversharp and Eberhard were further defined in an Inter-Company Agreement dated May 5, 1945 (R. 49-63).

During the year 1946 Eversharp and Eberhard withheld from the payments to Eterpen a total of $146,336.92 (R. 67). Subsequently, Eterpen received an administrative refund of $30,514.71, leaving a balance of $115,822.21 withheld and not refunded (R. 67). Eterpen's claim for refund of this sum withheld, plus accrued interest, was rejected by the Commissioner of Internal Revenue (R. 2-3), and on July 19, 1951, petitioner duly filed its petition in the Court of Claims (R. 1-4).

Eterpen's motion for summary judgment was denied by the Court of Claims, a cross-motion by the respondent was granted, and Eterpen's petition was dismissed on the ground that as a matter of law the form of the agreements negatived Eterpen's contention that it intended to effect a sale of the patents (R. 64-73).

Judge Madden registered a strong dissent in an excellent minority opinion (R. 73-75).

Reasons for Granting the Writ

I. The Decision of the Court Below is in Conflict with Numerous Decisions, including Decisions of this Court, the Courts of Appeals and the Tax Court.

The decision of the Court below is contrary to, and in conflict with, principles laid down in the following decisions of this Court: *Waterman* v. *Mackenzie*, 138 U. S. 252 (1891); *Littlefield* v. *Perry*, 88 U. S. 205 (1874); and *United States* v. *General Electric Co.*, 272 U. S. 476 (1926).

It is contrary to, and in conflict with, the following decisions by Courts of Appeals: *Green* v. *Le Clair*, 24 F. 2d 74 (7th Cir. 1928); *Hofferbert* v. *Briggs*, 178 F. 2d 743 (4th Cir. 1949); *Kavanagh* v. *Evans*, 188 F. 2d 234 (6th Cir. 1951); and *Allen* v. *Werner*, 190 F. 2d 840 (5th Cir. 1951).

It is also contrary to numerous decisions of the Tax Court, including *Parke, Davis & Co.* v. *Commissioner*, 31 B.T.A. 427 (1934); *Myers* v. *Commissioner*, 6 T. C. 258 (1946); *Kimble Glass Co.* v. *Commissioner*, 9 T. C. 183 (1947); *Dreymann* v. *Commissioner*, 11 T. C. 153 (1948); and *Taylor* v. *Commissioner*, 16 T. C. 376 (1951).

These cases—some involving patent issues and the others tax questions—all held that so-called license agreements which transferred the exclusive right to "make, use and vend" for the full term of a United States patent were in fact sales of the patent. The decision below improperly holds that such an agreement was a mere license.

II. The Court Below Committed Palpable Error in Holding as a Matter of Law that the Exclusive License Agreement was not an Assignment of the Patents.

The majority below committed a number of palpable errors in holding that the License Agreement did not effect a sale of the patents.

They drew wholly unjustified inferences from the existence of the option agreement as negativing an intent to make a sale. It is submitted that the existence of the option agreement was completely immaterial. It did nothing more than provide for an alternative method of payment and elimination of the security title retained by the petitioner. There was absolutely no other reason for its existence. A license rather than an assignment was utilized as a simple way of retaining record title to the patents to secure payment of the installments of the purchase price. This is a common and normal method of creating a purchase money mortgage upon the sale of a patent.

A second major error committed by the majority below was their assumption that Eversharp and Eberhard could not sue for infringement of the patents in their own names. The majority opinion states (R. 72) that a different result might have been reached had this right been transferred. It is perfectly clear from the record that *this right was in fact transferred,*[1] and for this misinterpretation of the agreements alone this petition should be granted.

A third major error committed by the majority below was the complete disregard of sworn testimony as to the intent of the parties. The question before the Court was the legal effect of the License Agreement and the related documents. Did the parties intend to transfer the property in

[1] R. 11, 24, 60-61. Brief, *infra*, pp. 21-23.

the patents? If the majority below felt that the documents were in any sense ambiguous it was their duty to refer to all the evidence in the record. Its failure to take into consideration the sworn statement of petitioner's attorney that the parties intended a transfer of the entire bundle of rights embodied in the patents is itself ground for the granting of this petition.

Other serious errors included unjustified inferences as to the purpose and effect of the December 1, 1946 "Memorandum of Agreement" and from the absence of a provision for application of royalties towards a fixed purchase price.

III. This Case Raises an Important Question of Federal Income Tax Law which has not been, but should be, Settled by this Court.

Patented inventions are responsible to a large degree for the growth of our economy. They are not ordinarily exploited by the inventor, for very few inventors have the money to practice their patents. A patent is therefore normally sold to others for exploitation, and because of its very nature, it is usually impossible for the parties to estimate its worth with sufficient accuracy to make it possible to agree upon a lump sum consideration. Patents are usually sold, therefore, on a royalty basis. An exclusive license to make, use and vend is a common way of effecting such a sale on installments, with the retention of security title.

The authorities have uniformly held that such a transaction constitutes a sale. Only the decision below, and the recent decision by the Court of Appeals for the Second Circuit in *Bloch* v. *United States*, 200 F. 2d 63 (1952); cert. den., 345 U. S. 935, April 13, 1953, are to the contrary.

The federal income tax consequences of such transactions are of considerable public importance, and the doubt and

uncertainty created by the decision below, which will necessarily lead to confusion and unnecessary litigation, should be resolved by this Court.

Specification of Errors to Be Urged

In deciding the case below the Court of Claims was guilty of palpable and obvious error:

(1) In failing to hold that the exclusive license agreement granted by petitioner to "make, use and vend" for the full term of certain United States patents, which transferred the entire ownership and control of the patents to the licensees and excluded the petitioner from any rights in the patents whatever except those incident to the collection of the stipulated consideration, was a sale for federal income tax purposes rather than a mere license for the use of the patents.

(2) In deciding this case contrary to, and in conflict with, *Waterman* v. *Mackenzie,* 138 U. S. 252 (1891); *Littlefield* v. *Perry,* 88 U. S. 205 (1874); *United States* v. *General Electric Co.,* 272 U. S. 476 (1926); *Green* v. *Le Clair,* 24 F. 2d 74 (7th Cir. 1928); *Kavanagh* v. *Evans,* 188 F. 2d 234 (6th Cir. 1951); *Parke, Davis & Co.* v. *Commissioner,* 31 B. T. A. 427 (1934); *Myers* v. *Commissioner,* 6 T. C. 258 (1946); *Kimble Glass Co.* v. *Commissioner,* 9 T. C. 183 (1947); *Dreymann* v. *Commissioner,* 11 T. C. 153 (1948); and *Taylor* v. *Commissioner,* 16 T. C. 376 (1951).

(3) In concluding that the option agreement negatived an intent to transfer ownership of the patents.

(4) In concluding that Eversharp and Eberhard could not sue for infringement in their own names.

(5) In disregarding the statement of petitioner's attorney that the parties intended to transfer the entire bundle of rights embodied in the patents.

(6) In drawing other unjustified inferences from the form of the License Agreement and the related documents.

Prayer

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued by this Court to the United States Court of Claims to the end that this case may be reviewed and determined by this Court.

Respectfully submitted,

WILLIAM A. PATTY,
Counsel for Petitioner,
20 Exchange Place,
New York 5, New York.

SHARON CLAY RISK,
Of Counsel.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 59

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA (FORMERLY ETERPEN, S. A.),
Petitioner,

vs.

THE UNITED STATES OF AMERICA

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

This brief is submitted in support of the attached petition for a writ of certiorari. A summary statement of the facts and the grounds upon which jurisdiction of this Court is invoked appear in the petition, and for the sake of brevity are not repeated here.

The Statutes and Regulations

Section 231 of the Internal Revenue Code imposes a tax upon certain specified items of income of nonresident foreign corporations, as follows:

> ". . . There shall be levied, collected, and paid for each taxable year, in lieu of the tax imposed by sections

13 and 14, upon the amount received by every foreign corporation not engaged in trade or business within the United States, from sources within the United States, as interest . . . dividends, rents, salaries, wages . . . compensations . . . or other fixed or determinable annual or periodical gains, profits, and income, a tax of 30 per centum of such amount, . . ."

The regulations under Section 231 provide that the tax is applicable to royalties, but not to the proceeds of sale of personal property:

". . . For the purposes of section 231(a), the term 'amount received' means 'gross income'. Specific items of fixed or determinable annual or periodical income are enumerated . . . but other fixed or determinable annual or periodical gains, profits, and income are also subject to the tax, as, for instance, royalties. . . ." (Reg. 111, Sec. 29.231-1(a))

". . . A nonresident foreign corporation is taxable under section 231(a) only on fixed or determinable annual or periodical gross income received from sources within the United States. Its taxable income does not include . . . profits derived from the sale within the United States of personal property or real property located therein. . . ." (Reg. 111, Sec. 29.231-2(a))

Section 144 provides for the withholding of the tax in the same manner as in the case of nonresident alien individuals, and Section 143 describes the manner in which withholding shall be made from the income of such persons as follows:

"All persons, in whatever capacity acting . . . having the control . . . or payment of . . . dividends, rents, salaries, wages . . . compensations . . . or other fixed or determinable annual or periodical gains, profits and income . . . of any nonresident alien individual . . . shall . . . deduct and withhold . . . a tax equal to 30 per centum thereof . . ."

The Regulations under Section 143 define fixed and determinable annual or periodical income to include royalties, but expressly exclude therefrom the proceeds of sale, as follows:

> "Only fixed or determinable annual or periodical income is subject to withholding. The Internal Revenue Code specifically includes in such income, interest, dividends, rent, salaries, wages . . . But other kinds of income are included, as, for instance royalties.
>
> ". . . The income derived from the sale in the United States of property, whether real or personal, is not fixed or determinable annual or periodical income. . . ." (Reg. 111, Sec. 29.143-2)

Section 119 defines income from sources within the United States to include royalties for the use of United States patents as follows:

> "*(a) Gross Income from Sources in United States.*—
>
> "The following items of gross income shall be treated as income from sources within the United States:
>
> • • • • • • •
>
> (4) *Rentals and Royalties.*—Rentals or royalties from property located in the United States or from any interest in such property, including rentals or royalties for the use of . . . patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other like property; . . ."

Argument

Under the above provisions of the Internal Revenue Code and the Regulations, it is perfectly clear that only royalties *for the use* of United States patents are subject to tax in the case of a nonresident foreign corporation, and that

payments on account of their *acquisition* are expressly exempt.[2]

The following decisions make it perfectly clear that the exclusive license agreement constituted a sale of the patents, and the royalties paid thereunder proceeds of the sale, and that the decision of the Court below to the contrary is clearly erroneous.

I. An Exclusive License to Make, Use and Vend Is a Sale

It is well settled that an exclusive license to make, use and vend for the full term of a United States patent constitutes an assignment of the patent. *Waterman* v. *Mackenzie*, 138 U. S. 252 (1891), is the controlling case. Although the question there involved was one of procedure in a patent litigation, the principles involved are equally applicable in the instant case. The opinion describes the nature of a patent and states unequivocally that any agreement which disposes of the right to make, use and vend a patent for its full term is an assignment regardless of the form of the agreement or the nomenclature used.

This Court said:

> "Every patent issued under the laws of the United States for an invention or discovery contains 'a grant to the patentee, his heirs and assigns, for the term of seventeen years, of the exclusive right to make, use and vend the invention or discovery throughout the United States and the Territories thereof.' Rev. Stat. § 4884.

---

[2] ". . . the statute itself makes the distinction and expressly declares a different rule for 'royalties for the use of a patent' and for payments received in consideration of 'the sale of personal property' which would necessarily include the sale of a patent. . . . The Treasury Regulations make this distinction clear." *Commissioner* v. *Celanese Corporation of America*, 140 F. 2d 339, 342 (D.C. Cir. 1944). Only royalties for the use of patents which consist "wholly of income" are taxed to nonresidents. Capital payments representing proceeds of sale are exempt. *Commissioner* v. *Wodehouse*, 337 U.S. 369, 393-394 (1949).

> The monopoly thus granted is one entire thing, and cannot be divided into parts, except as authorized by those laws. The patentee or his assigns may, by instrument in writing, assign, grant and convey, either, 1st, the whole patent, comprising the exclusive right to make, use and vend the invention throughout the United States; or, 2d, an undivided part or share of that exclusive right; or 3d, the exclusive right under the patent within and throughout a specified part of the United States. Rev. Stat. § 4898. A transfer of either of these three kinds of interests is an assignment, properly speaking, and vests in the assignee a title in so much of the patent itself, with a right to sue infringers; in the second case, jointly with the assignor; in the first and third cases, in the name of the assignee alone. Any assignment or transfer, short of one of these, is a mere license, giving the licensee no title in the patent and no right to sue at law in his own name for an infringement. . . .
>
> • • • • • • •
>
> "Whether a transfer of a particular right or interest under a patent is an assignment or a license does not depend upon the name by which it calls itself, but upon the legal effect of its provisions. . . ." (pp. 255-256)

The License Agreement in the instant case falls precisely within the first described alternative. Petitioner conveyed the exclusive right to make, use and vend the patents throughout the United States for their full terms. Petitioner retained nothing whatever after the conveyance except the right to receive the stipulated consideration, and a security title to guarantee receipt of the consideration.

How then did the majority below reach the conclusion that there was not a sale of the patents? They purported to find factors present which negatived the intent to make a transfer of the patents. Foremost among these they said was the option agreement. But the existence of such an

agreement does not affect in any way the rights granted under an exclusive license. *Green* v. *Le Clair*, 24 F. 2d 74 (7th Cir. 1928).

In *Green* v. *Le Clair* the latter granted to Sauerman the exclusive right to manufacture, use and sell in consideration of the payment of royalties, together with an option to purchase.

The Court of Appeals said:

> "In the agreement between Le Clair and Sauerman, neither the option to purchase the patent outright nor the provision that Sauerman may under certain conditions terminate the contract, qualifies the interest assigned. . . . Exercise of the option to purchase outright for a lump sum would free Sauerman from his obligations under the agreement— . . . the payment of royalty; the liability to forfeiture—but it could not add to the monopoly conferred upon Sauerman. . . ." (p. 77)

The facts in *Green* v. *Le Clair* are identical with the case at bar, the only difference being that there the option was incorporated in the exclusive license agreement itself. Yet the majority opinion below does not even refer to this case. [3]

---

[3] Not only did the majority below ignore completely the relevant and important *Green* v. *Le Clair* case, but they apparently relied instead upon *dicta* in two lower court decisions the holdings in which have no possible application. *Rhodes-Hochriem Mfg. Co.* v. *International Ticket Scale Corp.*, 57 F. 2d 713 (D.Del. 1932); *Federal Laboratories, Inc.* v. *Commissioner*, 8 T.C. 1150 (1947). The opinions in both cases contain *dicta* to the effect that if there are factors present in a license agreement which expressly negative the intent to transfer the patent, the transaction cannot be held the equivalent of an assignment. Petitioner does not question these *dicta*. Petitioner contends only that the presence of an option agreement does not negative the intent to make a sale, and these cases do not hold to the contrary. *Rhodes-Hochriem* held that an option to purchase a patent, standing alone, was not an assignment. *Federal Laboratories* held that a license which granted less than all three rights of manufacture, use and sale was not an assignment.

Kavanagh v. *Evans,* 188 F. 2d 234 (6th Cir. 1951), likewise involves the distinction between the transfer of the ownership of a patent as distinguished from the security title. There the taxpayer granted a license to manufacture, use and sell in consideration of stipulated lump sum payments. The contract further provided that upon the payment of the last agreed sum, the taxpayer, by proper assignment, would transfer the entire right, title and interest in the patent to the licensee. Despite the express reservation of record title, and the contemporaneous agreement to transfer it at a later date, the Court nevertheless held that the license agreement constituted an assignment and a sale.

The Court said:

> " . . . 'The *Waterman* case further points out, that whether the transfer of an interest or right under a patent is an assignment or a license, does not depend upon the name by which it is called, but upon the legal effect of its provisions. No particular form is required for an assignment but the instrument of transfer must be unambiguous and show a clear and unmistakable intent to part with the patent'. . . ." (p. 236)

The above cases appear to be the only ones in which the effect of a contemporaneous option agreement or a contemporaneous agreement to transfer record title at a later date have been considered. They make it perfectly clear, however, that such provisions have no effect upon the passing of the property in the patent, and no reason is apparent why a different result should be reached in the instant case. Such provisions are simply a means of providing for the elimination by the licensee of the licensor's security title upon the completion of payment for the patents.

Prior to the decision below the authorities were unanimous that an exclusive license to make, use and vend for the full term of a patent constitutes a sale for tax purposes.

See for example, *Kavanagh* v. *Evans, supra; Hofferbert* v. *Briggs,* 178 F. 2d 743 (4th Cir. 1949); *Parke, Davis & Co.* v. *Commissioner,* 31 B.T.A. 427 (1934); *Myers* v. *Commissioner,* 6 T. C. 258 (1946); *Kimble Glass Co.* v. *Commissioner,* 9 T. C. 183 (1947); *Dreymann* v. *Commissioner,* 11 T. C. 153 (1948); and *Taylor* v. *Commissioner,* 16 T. C. 376 (1951). The decision below and the recent decision of the Court of Appeals for the Second Circuit in *Bloch* v. *United States,* 200 F. 2d 63 (1952), cert. den. 345 U. S. 935, April 13, 1953, are the only exceptions to this unbroken line of authorities. This petition should be granted to correct the resulting conflict which can only result in confusion and unnecessary litigation.

II. The Court Below Committed Palpable Error in Holding as a Matter of Law that the Exclusive License Agreement was not a Sale

First Major Error—the Purpose and Effect of the Option Agreement

The principal ground given by the majority below for holding that the License Agreement did not effect a sale of the patents was their conclusion that when the License Agreement and the option agreement are considered together "they negative in clear and unmistakable terms . . . the contention by the taxpayer that it intended to effect the sale of the patents by means of the License Agreement alone" (R. 71).

This conclusion was based on the fact that in the option agreement Eterpen expressly warranted that it was "the sole and exclusive owner . . . of the patents," and that it had "the full right and power to assign and transfer the same" (R. 71). The majority argued that if the petitioner's position were correct and the License Agreement effected a sale, these words would become "meaningless"

and the option agreement itself "worthless" because Eterpen would have had nothing left to convey to Eversharp.

These arguments are wholly without merit or logic. What the majority below said, if analyzed carefully, is that they would ignore the nomenclature of the License Agreement to give effect to the true substance of the transaction, but not the nomenclature used in the option. They concede that the use of the terms "license" and "royalties" in the License Agreement must be ignored if the over-all substance of the transaction was a transfer of the entire patent monopoly. But they then take the completely inconsistent position that the same words in a related document—the option agreement—are of great significance and cannot be ignored. Thus, they attach importance to words in the option agreement entirely consistent with the License Agreement, although they concede that the nomenclature used in the License Agreement may be disregarded.

Another serious error is their conclusion that if the petitioner is right, and the exclusive license was in fact a sale, then the option agreement would serve no purpose—that upon the exercise of the option there would have been "nothing left to convey." Although the exercise of the option would not add to the monopoly conferred upon Eversharp (*Green* v. *Le Clair, supra*), it was by no means a "meaningless" or "worthless" act. The exercise of the option enabled Eversharp to free itself from continued installment payments and from liability to forfeiture. It severed Eterpen's only remaining tie to the patents by eliminating Eterpen's security title.

The Exclusive License Effected a Sale on Installments Secured by a Purchase Money Mortgage

The exclusive license to make, use and vend the pen and ink inventions was a complete sale. After the execution of

the License Agreement, Eterpen could not make or use or sell one of the pens, or a drop of the ink, in the United States. It had given up every vestige of ownership of the patents, save one—a security title to insure payment of the purchase price.

It could not give up this sole remaining right, for to have done so would have relegated it to the position of a general creditor. Had it given up this sole remaining right, the licensees could have sold the patents on any terms they chose, leaving Eterpen to rely simply upon their general credit for payment of the purchase price of the patents. Eterpen therefore reserved to itself record title—a mere security title—so long as any amount remained due on the purchase price.

The purpose of the option agreement was to cut off the one remaining right—security title—once payment had been made in full. The majority is completely in error when it says there was nothing left to convey. This is like saying that a mortgagee has nothing to convey. Until payment he retains a security title. When paid he gives a release. This was the one and only purpose of the option agreement—to provide an alternative lump sum method of payment and release of the security title.

The only reason why the agreements were couched in terms of license and option was to preserve the security title. There was no intent to hold back any part of the patent monopoly from the transfer. This is clear from the agreement itself—the rights granted were all-inclusive and the rights retained were merely protective—and from the statement by petitioner's attorney (R. 48). *There is no basis whatever for the majority's inference that the option agreement detracted to the slightest degree from the complete sale effected by the License Agreement.* On the contrary, the option agreement *strengthens* rather than *weakens* Eterpen's position that the operative intent was

to make a complete and irrevocable transfer of the patents. It supplied a method of release and satisfaction—a method of severing Eterpen's one remaining tie to the patents by elimination of its security title.

The License Agreement passed the property in the patents. *Waterman* v. *Mackenzie*, 138 U. S. 252 (1891). It is immaterial what provisions the parties made as to the security title. The licensee may have the option to acquire it upon payment of the stipulated consideration, as in *Green* v. *Le Clair, supra*, and the instant case. Or the licensor may agree to convey it upon completion of the stipulated payments as in *Kavanagh* v. *Evans, supra*, 235. Or the parties may deal with it separately from the original license. *Kronner* v. *United States*, 110 F. Supp. 730 (Ct. Cl. 1953). Retention or disposition of security title is of no consequence in determining whether there has been a disposition of the property in the patents. The majority below confused these two entirely unrelated questions and placed undue emphasis upon language in the option relating only to security title.

Second Major Error—That the Licensees Could Not Sue for Infringement in Their Own Names

Another major reason given by the majority below for holding that the petitioner did not intend to effect an assignment was their assumption that the License Agreement

> ". . . did not expressly confer upon the licensees the right to sue for infringement of the patents in their own names' '(R. 72).

This assumption is squarely contrary to the agreements.

Paragraph 4 of the License Agreement (R. 11) reads as follows:

> "Licensees, or either of them, may sue in Licensor's name, *or otherwise*, as they or either of them may deem fit, or as licensees, between them from time to time may

> agree in writing, for infringement and damages or otherwise pertaining to any and all of said pen and ink inventions and any money recovery shall be applied first to the reimbursement to the parties hereto of their expenses and costs therein, second to the payment to the Licensor of a sum equal to the royalties to which Licensor would have been entitled had the same made by the infringer been made by one of the Licensees, and any balance shall be retained by the Licensees." (Emphasis added)

This language is repeated in paragraph 29 (R. 29) which states that, upon the request of the licensees, Eterpen will execute and deliver to licensees a brief agreement suitable for recording which shall set forth the licensees' exclusive rights in the pen and ink inventions and

> "their right to sue in Licensor's name *or otherwise* to enforce the patent rights involved. . . ." (Emphasis added)

Such use of the words "or otherwise" is standard terminology in provisions relating to suits for infringement and has the well settled meaning that the licensee may sue in its own name. It could have no other meaning.

Furthermore, suits were to be brought *as Licensees* "may deem fit" or *as Licensees* "may agree". Eterpen reserved no rights whatever to determine whether infringement suits would be instituted.

Likewise, paragraph 4, which contains the provisions relating to the perfection, enforcement and protection of the patents, provides nowhere for infringement actions to be commenced by Eterpen. It provides instead that all costs and expenses for the perfection, enforcement and protection of the patents are to be borne by the licensees, and that all recoveries in excess of the stipulated royalties belong to the licensees. It merely gives Eterpen the right to *intervene*

in infringement actions—a provision which would be completely meaningless if it were necessary for the licensees to bring suit in Eterpen's name, or to join it in any infringement actions brought by licensees.

Finally, the Inter-Company Agreement,[4] which was signed in contemplation of the execution of the License Agreement and Option, also make it clear that the licensees had the power to sue for infringement in their own names. Part IV, B, (b) of that agreement states (R. 60-61):

> "Either of the parties may sue *in its own name* or in the names of both, or in the name of Licensor in said License Agreement, or otherwise, as either may deem fit, for infringement and damages. . . ." (Emphasis added)

The majority in its opinion, said that if the licensees had the right to bring suit in their own names it

> "would have been persuasive evidence that the taxpayer intended to convey all the rights it possessed. *Pike* v. *United States*, 101 F. Supp. 100." (R. 72)

Eterpen's licensees did in fact have the right to sue infringers in their own names. Since the majority assumed otherwise, although conceding the significance of such power, this palpable error alone constitutes grounds for the allowance of this petition.

Third Major Error—Disregard of Sworn Statement as to Intention of Parties

The majority below has completely ignored the sworn statement of Mr. Garrard Winston, attorney-in-fact for the

---

[4] The Inter-Company Agreement was entered into "for the purpose of declaring and setting forth, as between themselves [the licensees], their relative and respective rights, privileges, duties, obligations and intentions" under the License and Option Agreements (R. 50).

petitioner, submitted upon the motions, wherein he outlined the intent of the parties as follows (R. 48):

> "3. At the time the 'License Agreement' and the the 'Option Agreement' were entered into, *it was intended that the whole bundle of rights* under the patents and applications for patents set forth in Schedule A and B of the 'License Agreement', in the 'Licensee's Area' . . . *should be transferred to Eversharp and Faber* and should Eversharp and Faber through practical experience deem the patents commercially valuable they were to have the option by a lump sum payment to avoid future 'royalty' payments. The reason that the transfer was made in the form of a license rather than an assignment was to protect Eterpen in case there was a default on the payments. *We took the position that Eterpen had transferred its entire bundle of rights in the patent under the 'License Agreement'*. . . ." (Emphasis added)

The duty of the Court below was to determine the legal effect of the License Agreement and related documents. Petitioner moved for summary judgment on the ground that the documents were unambiguous and showed clearly an intent to sell the patents. The majority below found the agreements ambiguous, for they resorted to a number of tenuous arguments and inferences from the language of the agreements in reaching their conclusion. It was their duty, therefore, to consider all the evidence in the record. This they did not do. They ignored completely Mr. Winston's statement—the only direct evidence as to the intent of the parties.

This evidence was part of the record upon which the petitioner and respondent made cross-motions for summary judgment. There was no evidence whatever to the contrary. It was palpable error to ignore this material evidence, and its disregard by the majority below is itself grounds for the allowance of this writ.

Unjustified Inference from the December 1, 1946 Agreement

The majority below made a number of other wholly unjustified inferences. For example, they seized upon language in the December 1, 1946 Memorandum of Agreement as a factor negativing the intention to transfer the patent. They say that if an assignment had been intended, Eberhard would have become a joint assignee. They say this was not intended because in the December 1, 1946 Agreement Eberhard continued to be referred to as a "licensee" (R. 71). Here again the majority is in the inconsistent position of admitting that the word "licensee" in the License Agreement should be ignored in giving effect to the true substance of the transaction, but not in a related and wholly consistent document.

Eberhard *did* become a joint equitable assignee upon the execution of the License Agreement. But as between Eberhard and Eversharp, following the exercise of the option by Eversharp, the mortgage was still in effect. Eversharp had paid Eterpen in full. It stepped into Eterpen's shoes. It was required to pay nothing further to Eterpen, nor was Eberhard. Eberhard, however, was required to continue to make installment payments to Eversharp, and so long as anything remained due, Eversharp retained the security title.

The December 1, 1946 Agreement is entirely consistent with a complete transfer of the patents to the licensees. It simply defines the relations between the two purchasers. It speaks in the terms of "licensee" to be consistent. The use of the term "licensee" in that agreement is not one whit different from the use of the same term in the License Agreement itself. To draw any inference that there is any inconsistency, or to give any added weight to the nomenclature of the December 1, 1946 Agreement, is wholly unjustified.

The Option Agreement Had Some Purpose Other Than an Alternative Purchase Price

The majority below say they have difficulty in believing the taxpayer's contention that the sole purpose of the option agreement was to provide an alternative method of payment (R. 72). Their difficulty is caused by the fact that the taxpayer went to "great efforts to couch the license agreement in terms of licenses and royalties" (R. 72). The reason for the use of this terminology has been explained—this is a normal way to place a purchase money mortgage on a patent.

The majority goes on to say that the result for which the petitioner contends could have been achieved far more clearly and by much less cumbersome means if one agreement had been used. Can they seriously believe that the legal effect of a transaction depends upon whether it is effected by one or more agreements? It is submitted that the agreements involved are extremely well prepared. They were drafted by experts in the field of patent law representing both the petitioner and the licensees. They used customary forms and normal language to accomplish the result desired. It is a real question whether they would have been simplified or made more complicated had they been combined in one agreement.

But this is completely immaterial in any case. What is important is the rights transferred. Even the intent to make a sale or a license is not conclusive. In fact, the taxpayers in many of the cases assumed that true license agreements had been entered into and that the payments under them were true royalties. They paid taxes on them as royalties. This did not prevent a refund when the true nature of the transactions was determined.[5]

---

[5] *Myers* v. *Commissioner*, 6 T.C. 258 (1946); *Hessert* v. *Commissioner*, 6 T.C.M. 1190 (1947); *Thompson* v. *Johnson* (D.C. S.D.N.Y. 1950);

The only intent that is important is the intent that goes to the extent of the rights transferred. Where, as in the instant case, there was an intent to transfer all rights except a security title, there has been a sale for tax purposes, regardless of the nomenclature used, the number of agreements involved, or even what the parties may have thought were the legal consequences of their actions.

Reliance Upon Absence of a Provision for Application of Royalties Towards a Fixed Purchase Price

Another factor relied upon by the majority below in reaching their conclusion was the License Agreement did not transfer beneficial ownership of the patents was the absence of a provision applying the royalty payments towards a fixed purchase price (R. 72). Any such conclusion is completely unjustified. Whether a patent is sold on a royalty basis, or for a lump sum, and if on a royalty basis, whether the payments of royalty are to be applied against the purchase price, are entirely matters of negotiation between the parties.

The option in the instant case was only for ten months, so that royalties, if any, paid during that period would represent only a small portion of the value of the patent. In fact, no royalties whatever were paid during the original option period (R. 48). Under these circumstances application of the royalties to the purchase price would have been of little significance. In fact, the absence of a provision for the application of royalties to an option price ordinarily puts pressure upon the purchaser to exercise the option promptly, and in the instant case shows a desire on the part of the taxpayer to force the licensees to exercise the option and thus eliminate installment payments.

50-2 U.S.T.C. Par. 9428; *Pike* v. *Commissioner*, 101 F. Supp. 100 (D. Conn., 1951); *Lamar* v. *Granger*, 99 F. Supp. 17 (W.D. Pa., 1951).

Reliance on Absence of a Reason for Disregarding the Form of the Agreements

Another factor relied upon by the majority below was that:

> "No valid reason has been put forth to warrant our disregarding the significance of either the language or of the type of agreement selected by the taxpayer" (R. 72-73).

This statement is erroneous on two scores. In the first place, a reason has been given. The agreements were couched in the form of a license and option because this is a normal way to sell a patent on the installment basis, retaining a purchase money mortgage.

But even if no such reason had been given, none is necessary. No reason was given for ignoring the form of the agreement in any of the many other cases relied upon by the taxpayer in which a license agreement was held to be in fact a contract of sale. The Court is bound to give effect to the substance of an agreement, regardless of its form or the nomenclature used.

Conclusion

It is submitted that the decision by the majority below is based upon unsubstantial grounds of form and terminology. As Judge Madden so aptly put it in his dissenting opinion, *"I find nothing which indicates a license agreement except labels and words"* (R. 75).

The decision below is squarely in conflict with the principles laid down by this Court in *Waterman* v. *Mackenzie, supra,* and a long and uniform line of decisions by the Courts of Appeals and the Tax Court of the United States. The majority's conclusion could have been reached only because they ignored uncontradicted evidence of the intention

of the parties to dispose of the entire bundle of rights involved in the patents, and because they misinterpreted the agreements themselves, which clearly gave the licensees the right to sue for infringement in their own names.

An inventor ordinarily is not in a position to practice his own patent but sells it to others for exploitation. At the hearings before the Senate Committee on Finance on the 1950 Revenue Act, Mr. C. E. Earle, secretary-treasurer of the Council for Independent Business, testified in this connection:

> "It is a well-known fact that very few inventors have the money to practice their patents. In order to profit from the patent, the inventor must either sell it or license its use—usually an exclusive license which the courts have held is equivalent to a sale." (Hearings before the Senate Committee on Finance on H.R. 8920, 81st Cong., 2nd Session, pp. 603-604.)

And because, by the very nature of a patent, its value is usually too uncertain to make it possible for the parties to agree upon an over-all sale price, it is normally sold on a royalty basis. Only in this manner can the inventor obtain a fair price. "The parties are not required to be clairvoyant or prescient and determine beforehand a lump amount; it is a matter of speculation. The patent may be commercially marketable or it may not be and the parties account for this risk by providing for installment payments based on a percentage of sales." *Lamar* v. *Granger*, 99 F. Supp. 17, 38 (W.D. Pa. 1951).

This was exactly the situation in the instant case. The patents were sold on an installment basis, record title being retained only for security purposes. There is not one iota of evidence in the record to support the majority's conclusion that as a matter of law a sale was not intended or effected by the License Agreement.

The question is an important one involving the application of principles laid down by this Court in *Waterman* v. *Mackenzie* and this Court should resolve the conflict of the decision below with the many authorities cited herein, and correct the palpable errors committed by the Court below, in order to prevent confusion and unnecessary litigation in the administration of the Federal income tax law.

WHEREFORE, your petitioner respectfully prays that this petition for a writ of certiorari be granted.

Respectfully submitted,

WILLIAM A. PATTY,
Counsel for Petitioner,
20 Exchange Place,
New York 5, New York.

SHARON CLAY RISK,
Of Counsel.

(8060)

INDEX

	Page
Opinion below	1
Jurisdiction	1
Question presented	2
Statute and regulations involved	2
Statement	2
Argument	7
Conclusion	12
Appendix	13

CITATIONS

Cases:	
Allen v. *Werner*, 190 F. 2d 840	11
Bloch v. *United States*, 200 F. 2d 63, certiorari denied, 345 U. S. 935	8, 10
Commissioner v. *Wodehouse*, 337 U. S. 369	8–10, 12
Green v. *Le Clair*, 24 F. 2d 74	11
Herwig v. *United States*, 105 F. Supp. 384	12
Hofferbert v. *Briggs*, 178 F. 2d 743	11
Kavanagh v. *Evans*, 188 F. 2d 234	11
Kimble Glass Co. v. *Commissioner*, 9 T. C. 183	11
Kronner v. *United States*, 110 F. Supp. 730	12
Littlefield v. *Perry*, 21 Wall. 205	12
United States v. *Gen. Elec. Co.*, 272 U. S. 476	12
Waterman v. *Mackenzie*, 138 U. S. 252	11, 12
Statute:	
Internal Revenue Code:	
Sec. 117	12
Sec. 119 (26 U. S. C. 1946 ed., Sec. 119)	13
Sec. 143 (26 U. S. C. 1946 ed., Sec. 143)	13
Sec. 144 (26 U. S. C. 1946 ed., Sec. 144)	14
Sec. 211 (26 U. S. C. 1946 ed., Sec. 211)	8, 9
Sec. 231 (26 U. S. C. 1946 ed., Sec. 231)	7, 8, 14
Miscellaneous:	
Treasury Regulations 111:	
Sec. 29.143–2	15
Sec. 29.231–1	16
Sec. 29.231–2	16

264231—53——1

In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 59

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA (FORMERLY ETERPEN, S. A.), PETITIONER

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The majority and dissenting opinions of the Court of Claims (R. 64–75) are reported at 108 F. Supp. 100.

JURISDICTION

The judgment of the Court of Claims was entered on November 4, 1952 (R. 75). Motion for rehearing was denied February 3, 1953 (R. 76). The petition for a writ of certiorari was filed May 4, 1953. The jurisdiction of this Court is invoked under 28 U. S. C. 1255.

QUESTION PRESENTED

Whether the court below erred in holding that payments made during 1946 to petitioner, a nonresident foreign corporation, are taxable under Section 231 (a) (1) of the Internal Revenue Code as royalties for the use of a patent.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the statutes and Treasury Regulations involved are set forth in the Appendix, *infra*, pp. 13–16.

STATEMENT

Petitioner, the taxpayer, brought suit in the Court of Claims for recovery of $115,822.21 in income taxes alleged to have been erroneously withheld in 1946 by Eversharp, Inc., and Eberhard Faber Corporation from payments due taxpayer for the use of certain United States patents (R. 64). On motions for summary judgment filed by both parties, taxpayer's petition was dismissed (R. 75).

The relevant facts as reflected by the pleadings, affidavits, and exhibits and as outlined by the court below (R. 65–67) may be summarized as follows:

Taxpayer is an Argentine corporation not engaged in trade or business within the United States (R. 64). It was the possessor of certain United States patents and pending patent applications on a ball pointed fountain pen known as

the "Biro Pen" and on a pulpy ink or writing paste for use in that pen (R. 65).

On May 18, 1945, taxpayer entered into a "License Agreement" R. 7–25) with Eversharp, Inc., and Eberhard Faber Corporation under which it granted to those companies, jointly, the exclusive "right and license" under its United States patents "to make, use and vend," throughout the United States, Hawaii and Alaska and for the full life of the patents, the devices and materials made from and in accordance with the patents, subject to certain conditions and rights of cancellation and termination (R. 9). Under the agreement the licensees were to pay "as royalties" to the licensor, at the end of each calendar quarter of each year, a sum of money equivalent to 5¼ percent of their net sales prices, less certain costs and expenses incurred by the licensees (R. 15). The obligations of the licensees to pay such royalties were to be joint and several (R. 21–22) and the licensees could deduct from royalty payments any amounts required by the laws of the United States to be withheld for taxes (R. 19). The licensees, by joint action only, could sublicense to others (R. 12) but the sublicenses were to contain substantially the same cancellation and termination provisions as the licensing agreement (R. 13), as well as similar provisions regarding the keeping of records of manufacture and sale of the patented articles and

products (R. 19). The licensees could sue in taxpayer's name and any money recovered was to be applied first to the reimbursement of expenses and costs, second to the payment to taxpayer of royalties on the infringing sales, and the balance to the licensees (R. 65). The licensing agreement could not be assigned by the licensees or either of them without the written consent of taxpayer and the other licensee, except under certain conditions (R. 21). Taxpayer was to do all acts, matters and things which might be necessary to keep the patents or any improvements on them in full force and effect (R. 11) and, when called upon to do so by the licensees, was to take all steps, to do all acts, and to execute, verify and deliver any and all papers as the licensees might deem expedient, necessary or advisable (R. 11–12). Taxpayer could terminate the licensing agreement as to a licensee which did not pay any amount due within 30 days, or which completely discontinued the sale of all such pen and ink inventions for a period of at least three months, or which filed a petition in bankruptcy or otherwise acknowledged itself to be or was held to be insolvent (R. 19–20). Either of the licensees could "relinquish" its rights and terminate the agreement with respect to itself after the agreement had been in effect 7½ years (R. 21).

Simultaneously with and in consideration of the execution of the "License Agreement," taxpayer entered into an "Option" agreement (R. 33–39)

under which it gave the licensees, individually and jointly, an exclusive option to purchase, for the lump sum of $1,500,000, the entire right, title and interest in and to the patents and patent applications covered by the license agreement for the area embraced in the license agreement (R. 33–34, 37).[1] In this option agreement taxpayer warranted that "it now is and at the date of the exercise of the option will be the sole and exclusive owner of the entire right, title and interest in and to all of said patents and applications, free of encumbrances," and that "it has and will then have full right and power to assign and transfer the same" (R. 36). By its terms the option expired March 1, 1946 (R. 37–38), but it was subsequently extended by mutual consent of the parties (R. 66).

On December 1, 1946, Eversharp and taxpayer executed an agreement (R. 40–45) under which Eversharp, on its own behalf, exercised the option and purchased from taxpayer the patents and patent applications covered by the license agreement. Under this agreement taxpayer assigned its full right, title and interest to Eversharp

[1] On May 5, 1945, in contemplation of the execution of the license agreement and option agreements with taxpayer, Eversharp and Eberhard Faber entered into an agreement setting forth their respective rights and duties as joint licensees. (See R. 49–62.) Among other things, the agreement provided that Eversharp would produce the pens and ink to be sold by Eberhard Faber and that the latter might acquire up to 25 percent of Eversharp's production (R. 51).

(R. 42) and the license was to continue in full force and effect "with Eversharp supplanting Eterpen as the owner of said United States patent rights, and with Faber operating as Eversharp's exclusive licensee thereunder" (R. 43). Although the option agreement called for a purchase price of $1,500,000, taxpayer accepted $1,100,000 in view of the fact that the "royalty payments" by Eversharp and Eberhard Faber for 1946, the first year of production, had exceeded $450,000[2] (R. 49, 66). Since Eberhard Faber did not desire to participate in the purchase of the patents, Eversharp, by means of a supplemental agreement, consented to continue to recognize Eberhard Faber's rights as licensee under the patents (R. 45–46, 66).

Shortly after the execution of the license agreement on May 18, 1945, both taxpayer and Eberhard Faber requested a ruling by the Commissioner as to whether the payments under the license agreement were subject to withholding tax at the source under Sections 143 (b) and 144 of the Internal Revenue Code. Pending this decision, Eversharp elected to withhold 30 percent of the amount of the payments to taxpayer during 1946. On December 22, 1947, the Commissioner ruled that the payments under the license agreement were in fact royalties and subject to

[2] The purchase price of $1,100,000 included $50,000 for the Canadian patent rights which had been licensed to Twoco Corporation, Ltd., a subsidiary of Eversharp (R. 43, 66).

withholding tax at the source. The Commissioner also determined, upon grounds not disclosed by the record, that $30,514.71 of the amount previously withheld should be refunded to taxpayer. Thereafter, taxpayer filed claims for refund of the balance of the withheld tax ($115,822.21), contending that the payments under the license agreement constituted payments of the purchase price for patent rights allegedly "purchased" jointly by Eversharp and Eberhard Faber. The claims for refund were rejected and this suit for recovery of the tax followed. (R. 66–67.)

The Court of Claims held that the license agreement constituted a license of the right to use the patents, rather than a sale of the patents, and that the payments made thereunder were accordingly taxable to taxpayer, and subject to withholding tax at the source as royalties for the use of the patents (R. 67–73).

ARGUMENT

The answer to the question presented, *viz,* whether the payments made to taxpayer, a nonresident corporation, under a licensing agreement during 1946 are taxable to it under Section 231 (a) (1) of the Internal Revenue Code, *infra,* pp. 14–15, as royalties for the use of certain patents, is dependent upon whether the licensing agreement, construed in the light of a simultaneously executed option-to-purchase agreement and other related

documents, should be treated as a sale of the patents or as a license to use them. Thus, the case turns on its own peculiar facts, and there is no substance in taxpayer's assertion (Pet. 7–8) that the decision of the court below creates general doubt and uncertainty in the income tax field which should be resolved by this Court. Moreover, the decision of the court below is in harmony with the decision of this Court in *Commissioner* v. *Wodehouse*, 337 U. S. 369, and is also supported by the decision of the Court of Appeals for the Second Circuit in *Bloch* v. *United States*, 200 F. 2d 63, certiorari denied, 345 U. S. 935. And it is not in conflict with the decision of any other court rendered since the *Wodehouse* case was decided.

In the *Wodehouse* case, this Court held that lump sum payments received by a nonresident alien individual, under an agreement granting exclusive serial or book rights throughout the United States during the life of the copyrights in certain stories, constituted income taxable as royalties (and thus were not to be considered the proceeds of a sale) under Section 211 (a) (1) (A) of the Internal Revenue Code, of which Section 231 (a) (1), involved here, is a corollary covering nonresident foreign corporations. In that case, the taxpayer likewise contended that the agreements were outright sales rather than licensing agreements and that the proceeds were not therefore taxable, but this Court held that

the amounts received under those agreements were not of the character that Congress intended should be excluded from the taxable income of the nonresident recipients. Thus, by holding that the amounts received were royalties within the meaning of Section 211, this Court held, in effect, that they were not the proceeds of sales for taxation purposes. And it is clear that the effect of this Court's holding in that case is that Congress intended that no agreement which purports to be a licensing agreement with respect to copyrights and patents shall be treated as a sale, so as to exclude the amount received from the taxable income of a nonresident, so long as the income taxes thereon can be easily and readily withheld and collected at the source, even though the agreement might be treated as a sale or an assignment for other purposes.

In construing the statute to that effect, the Court said, *inter alia,* that it was the difficulty of ascertaining income derived from sales of property by nonresident aliens not engaged in business in this country which induced Congress to relieve such nonresident aliens of tax on gains from the sale of property. The Congressional purpose, said the Court, was "to limit future taxes on nonresident alien individuals to those readily collectible." (See pp. 388–389.) Taxes on the payments involved in the present case were as "readily collectible" at the source (if not more so) as were the taxes on the lump sum payments involved in

the *Wodehouse* case, and, moreover, the payments received by the taxpayer in this case were payments which the parties to the agreement themselves treated as royalties for the use of the patents, rather than as part of the purchase price on a sale of the patents. In the circumstances, there is no more and even less reason to construe the agreement involved here as a sale than there was to treat the transactions involved in the *Wodehouse* case as such.

The decision of the court below likewise finds substantial direct support in *Bloch* v. *United States, supra.* The *Bloch* case involved an agreement under which a nonresident alien individual granted to a New Jersey corporation full, sole, and exclusive license and authority to make, use, and vend the subject of the patent involved for its duration, in the United States and its territories and possessions. Thus, the question there presented was identical with the question presented here, except, as in the *Wodehouse* case, the taxpayer was an individual instead of a corporation, which caused the case to arise under Section 211 rather than Section 231. The Second Circuit followed this Court's pronouncements in the *Wodehouse* case to the effect that Congress intended to tax all of those payments which purported to be royalties and which were readily withholdable at their sources, and in reaching the conclusion that the payments were taxable, took

the position that the considerations which governed this Court's decision in *Waterman* v. *Mackensie,* 138 U. S. 252, an infringement suit, were not controlling in the field of taxation.

There is, therefore, no merit in taxpayer's contention (Pet. 6–7, 18–28) that the court below committed error in holding that the license agreement herein did not effect a sale of the patent, since under the holding of this Court, and that of the Second Circuit, the royalties were taxable in any event. And even if the question before the court below had been confined strictly to the legal effect of the license agreement and related documents, its decision would still be correct, since its conclusion that the agreement constituted a license rather than a sale was compelled by the language of the license and option agreements.

The cases of *Green* v. *Le Clair,* 24 F. 2d 74 (C. A. 7); *Hofferbert* v. *Briggs,* 178 F. 2d 743 (C. A. 4); *Kavanagh* v. *Evans,* 188 F. 2d 234 (C. A. 6); and *Allen* v. *Werner,* 190 F. 2d 840 (C. A. 5), asserted by taxpayer as being in conflict with the present decision (Pet. 5, 16–18), all involved citizens of the United States. *Green* v. *Le Clair, supra,* did not even involve a tax question. Of the Tax Court cases cited by taxpayer (Pet. 5, 18), only one involved the taxation of a nonresident alien (*Kimble Glass Co.* v. *Commissioner,* 9 T. C. 183) and that case was decided

prior to this Court's decision in the *Wodehouse* case. The court below has itself recognized that the taxation of a nonresident alien poses a different problem from the treatment properly to be accorded to transactions of citizens under Section 117 of the Code (26 U. S. C. (1946 ed.) 117). See *Kronner* v. *United States,* 110 F. Supp. 730 (C. Cls.); *Herwig* v. *United States,* 105 F. Supp. 384 (C. Cls.). The cases of *Waterman* v. *Mackenzie,* 138 U. S. 252; *Littlefield* v. *Perry,* 21 Wall. 205; and *United States* v. *Gen. Elec. Co.,* 272 U. S. 476, also cited by taxpayer as being in conflict with the decision below (Pet. 5), involved considerations entirely apart from tax questions. In the circumstances, the reasoning entering into the conclusions there reached is not controlling here.

CONCLUSION

The decision of the court below is correct, there is no conflict of decisions, and further review is not warranted. The petition for a writ of certiorari should therefore be denied.

Respectfully submitted.

OSCAR H. DAVIS,
Acting Solicitor General.
H. BRIAN HOLLAND,
Asistant Attorney General.
ELLIS N. SLACK,
MELVA M. GRANEY,
Special Assistants to the Attorney General.

JULY 1953.

APPENDIX

Internal Revenue Code:

SEC. 119. INCOME FROM SOURCES WITHIN UNITED STATES.

(a) *Gross Income from Sources in United States.*—The following items of gross income shall be treated as income from sources within the United States:

* * * * *

(4) *Rentals and royalties.*—Rentals or royalties from property located in the United States or from any interest in such property, including rentals or royalties for the use of or for the privilege of using in the United States, patents, copyrights, secret processes and formulas, good will, trade-marks, trade brands, franchises, and other like property; and

(5) *Sale of real property.*—Gains, profits, and income from the sale of real property located in the United States.

(6) *Sale of personal property.*—For gains, profits, and income from the sale of personal property, see subsection (e).

* * * * *

(26 U. S. C. 1946 ed., Sec. 119.)

SEC. 143. WITHHOLDING OF TAX AT SOURCE.

* * * * *

(b) [As amended by Secs. 108 (a) and 160 (a) (2) of the Revenue Act of 1942, c. 619, 56 Stat. 798.] *Nonresident Aliens.*—All persons, in whatever capacity acting, * * * having the control, receipt, custody, disposal, or payment of interest (except interest on deposits with persons

carrying on the banking business paid to persons not engaged in business in the United States), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income (but only to the extent that any of the above items constitutes gross income from sources within the United States), of any nonresident alien individual, or of any partnership not engaged in trade or business within the United States and composed in whole or in part of nonresident aliens, shall * * * deduct and withhold from such annual or periodical gains, profits, and income a tax equal to 30 per centum thereof, * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 143.)

SEC. 144. [As amended by Secs. 108 (a) and 160 (a) (3) of the Revenue Act of 1942, *supra.*]—PAYMENT OF CORPORATION INCOME TAX AT SOURCE.

In the case of foreign corporations subject to taxation under this chapter not engaged in trade or business within the United States, there shall be deducted and withheld at the source in the same manner and upon the same items of income as is provided in section 143 a tax equal to 30 per centum thereof, * * *.

(26 U. S. C. 1946 ed., Sec. 144.)

SEC. 231. TAX ON FOREIGN CORPORATIONS.

(a) [As amended by Secs. 107 and 160 (e) of the Revenue Act of 1942, *supra*]—*Nonresident Corporations.*—

(1) *Imposition of tax.*—There shall be levied, collected, and paid for each taxable year, in lieu of the tax imposed by sec-

tions 13 and 14, upon the amount received by every foreign corporation not engaged in trade or business within the United States, from sources within the United States as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, a tax of 30 per centum of such amount, * * *.

* * * * *

(26 U. S. C. 1946 ed., Sec. 231.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.143–2. *Fixed or Determinable Annual or Periodical Income.*—Only fixed or determinable annual or periodical income is subject to withholding. The Internal Revenue Code specifically includes in such income, interest, dividends, rent, salaries, wages, premiums, annuities, compensations, remunerations and emoluments. But other kinds of income are included, as, for instance, royalties.

Income is fixed when it is to be paid in amounts definitely predetermined. Income is determinable whenever there is a basis of calculation by which the amount to be paid may be ascertained. The income need not be paid annually if it is paid periodically; that is to say, from time to time, whether or not at regular intervals. * * * The income derived from the sale in the United States of property, whether real or personal, is not fixed or determinable annual or periodical income. * * *

SEC. 29.231–1. *Taxation of Foreign Corporations.*—* * *

(a) *Nonresident foreign corporations.*—* * * For the purposes of section 231 (a), the term "amount received" means "gross income." Specific items of fixed or determinable annual or periodical income are enumerated * * * but other fixed or determinable annual or periodical gains, profits, and income are also subject to the tax, as, for instance, royalties. * * *

* * * * * *

SEC. 29.231–2. *Gross Income of Foreign Corporations.*—* * *

(a) *Nonresident foreign corporations.*—A nonresident foreign corporation is taxable under section 231 (a) only on fixed or determinable annual or periodical gross income received from sources within the United States. Its taxable income does not include * * * profits derived from the sale within the United States of personal property or real property located therein.

* * * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1939

OCT 2 1953
HAROLD B. WILLEY, Clerk

Supreme Court of the United States

OCTOBER TERM, 1953.

No. 59.

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA
(Formerly Eterpen, S. A.),
Petitioner,

vs.

THE UNITED STATES.

REPLY BRIEF FOR THE PETITIONER

WILLIAM A. PATTY,
Counsel for Petitioner,
20 Exchange Place,
New York 5, New York.

SHARON CLAY RISK,
Of Counsel.

Pandick Press, Inc., 22 Thames St., New York 6, N. Y., U. S. A.

INDEX.

SUBJECT INDEX.

PAGE

Respondent's First Point. "* * * No Substance in Taxpayer's Assertion That the Decision of the Court Below Creates General Doubt and Uncertainty in the Income Tax Field Which Should Be Resolved by This Court" (Br. 8) 1

Respondent's Second Point. "The Decision of the Court Below Is in Harmony With the Decision of This Court in *Commissioner* v. *Wodehouse* * * *" (Br. 8) 2

Respondent's Third Point. "* * * The Decision of the Court Below Is * * * Also Supported By the Decision of the Court of Appeals for the Second Circuit in *Bloch* v. *United States* * * *" (Br. 8) 5

Respondent's Fourth Point. "* * * The Effect of This Court's Holding in That Case [*Wodehouse*] Is That Congress Intended That No Agreement Which Purports to Be a Licensing Agreement With Respect to Copyrights and Patents Shall be Treated as a Sale * * * So Long as the Income Taxes Thereon Can Be Easily and Readily Withheld * * *" (Br. 9) 5

Respondent's Fifth Point. "* * * The Payments Received By the Taxpayer * * * Were Payments Which the Parties to the Agreements Themselves Treated as Royalties * * *" (Br. 10) 6

The Brief for the Respondent Has Attempted to Answer None of the Taxpayer's Arguments 7

Conclusion 8

Table of Cases Cited.

Cases:

	PAGE
Bloch v. *United States*, 200 F. 2d (1952), cert. den. 345 U. S. 935, April 13, 1953	5, 8
Eben H. Carruthers v. *United States*, 53-1 USTC ¶9316 (D. C. Ore. 1953)	2
Commissioner v. *Celanese Corporation of America*, 140 F. 2d 339 (D. C. Cir. 1944)	4, 5
Commissioner v. *Wodehouse*, 337 U. S. 369, (1949)	2, 3, 4 5, 6, 8
General Aniline & Film Corporation v. *Commissioner*, 139 F. 2d 759 (2d Cir. 1944)	4, 5
General Spring Corporation v. *Commissioner*, 12 TCM 847, 853 (1953) [CCH Dec. 19, 822 (M)]	2
Kimble Glass Co. v. *Commissioner*, 9 T. C. 183 (1947)	4, 5
Kronner v. *United States*, 110 F. Supp. 730 (Ct. Cl. 1953)	2
Sabatini v. *Commissioner*, 32 BTA 705 (1935) affirmed 98 F. 2d 753 (1938)	3, 4
Waterman v. *Mackenzie*, 138 U. S. 252 (1891)	7

Statutes and Other Authorities Cited.

Internal Revenue Code,	
Section 117(a)(1)(C)	4
Section 211(a)(1)(B)	4
Revenue Act of 1950,	
Section 210(a)	4
Section 213(a)	4
Revenue Act of 1936,	
Section 211(a)	3
Income Tax Unit Ruling,	
I. T. 1232, I-1 C. B. 207 (1922)	3
Treatise:	
Neil F. Phillips, United States Taxation of Nonresident Aliens and Foreign Corporations, Chapter III, page 84	2

Supreme Court of the United States

OCTOBER TERM, 1953

No. 59.

ETERPEN FINANCIERA SOCIEDAD DE RESPONSABILIDAD LIMITADA (Formerly Eterpen, S. A.),

Petitioner,

vs.

THE UNITED STATES

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

REPLY BRIEF FOR THE PETITIONER.

The brief in opposition to the petitioner's application for a writ of certiorari makes the five following points:

RESPONDENT'S FIRST POINT.

"* * * No Substance in Taxpayer's Assertion That the Decision of the Court Below Creates General Doubt and Uncertainty in the Income Tax Field Which Should Be Resolved by This Court" (Br. 8).

The decision below, as the result of the numerous errors pointed out in petitioner's main brief, reaches the conclusion that the existence of a contemporaneous option agreement prevents an exclusive license agreement from effecting a sale.

The vehicle of the exclusive license agreement is used frequently for the transfers of patents both by citizens and nonresident aliens. *Kronner* v. *United States,* 110 F. Supp. 730, 733-734 (Ct. Cl. 1953); *Eben H. Carruthers* v. *United States,* 53-1 USTC ¶ 9316 (D. C. Ore. 1953); *General Spring Corporation* v. *Commissioner,* 12 TCM 847, 853 (1953) [CCH Dec. 19, 822 (M)]; PHILLIPS, UNITED STATES TAXATION OF NONRESIDENT ALIENS AND FOREIGN CORPORATIONS, Chapter III, page 84 (1952), and numerous cases cited at pages 16-18 of petitioner's main brief. The completely unwarranted conclusion of the Court below thus creates general doubt and uncertainty in the income tax field both as to citizens as well as to nonresident aliens.

RESPONDENT'S SECOND POINT.

"The Decision of the Court Below Is in Harmony With the Decision of This Court in *Commissioner* v. *Wodehouse* * * *" (Br. 8).

The decision of the Court below is in harmony with the *Wodehouse* decision only in that the nonresident alien taxpayer was held subject to tax in both cases. The two situations are clearly distinguishable. The *Wodehouse* case involved a transfer of a *part* of a *copyright.* The instant case involves the transfer of the *whole* of a *patent.* Congress had tacitly approved by reenactment of the applicable taxing statutes the Treasury's position that the consideration received by a nonresident alien for the transfer of a *part* of a *copyright* is subject to United States tax. *On the contrary,* Congress has tacitly approved by reenactment the Regulations and the numerous decisions of the Courts of Appeal and of the Tax Court, that the consideration received by a nonresident alien for the transfer of *all the rights* under a *patent* is *not* subject to United States income tax.

The *Wodehouse* case turned upon the fact that the consideration for the transfer of a *part* of a *copyright* (serial and book rights) had been subject to withholding as a royalty at the time of the enactment of the Revenue Act of 1936. That Act, although it exempted nonresident aliens for the first time from tax on the sale of personal and real property in the United States, continued to impose a tax upon all income which had previously been subject to withholding. The payments to *Wodehouse* were therefore taxable under the identical sections of the revenue acts applicable in that case. In reaching this result this Court relied upon the fact that the applicable Treasury Rulings required withholding, and that this position had been sustained in the only pending court case involving the question at the time the 1936 Act became effective. Both the majority and dissenting opinions assumed that the result would have been otherwise had the transaction involved been a transfer of an entire copyright (pp. 382 and 407). Application of the *Wodehouse* case to the transfer of an *entire* patent is therefore unwarranted.

The legislative history of the provisions taxing nonresident aliens is entirely different as respects transfers of patents. Whereas this Court found that the applicable Treasury Ruling as to the transfer of a *part* of a *copyright* required withholding at the time of the enactment of §211(a) of the Revenue Act of 1936, the precursor of the provisions applicable in that case, the situation is otherwise as to the transfer of an entire patent. I. T. 1232, I-1 C. B. 207 (1922), involving the transfer of an entire patent in consideration of installment payments, held that withholding was *not* required.

This Court also relied on the fact that the only case involving the taxability of a *part* of a *copyright* (*Sabatini* v. *Commissioner*, 32 BTA 705 (1935)) was on appeal at the

time of the enactment of the Revenue Act of 1936, and was affirmed shortly thereafter (98 F. 2d 753 (2d Cir. 1938)), prior to the enactment of the Internal Revenue Code under which the payments involved in the *Wodehouse* case were taxable. The situation is entirely different in the case of patents. There was no case involving the transfer of a patent pending at the time of the enactment of the Revenue Act of 1936. The law and the Regulations were clear that the proceeds of *sales* of personal property by a nonresident alien were not subject to tax. Furthermore, all the cases decided prior to the decision below had consistently held that the proceeds of the transfer of an entire patent by a nonresident were not subject to tax. *General Aniline & Film Corporation* v. *Commissioner,* 139 F. 2d 759 (2d Cir. 1944); *Commissioner* v. *Celanese Corporation of America,* 140 F. 2d 339 (D. C. Cir. 1944); and *Kimble Glass Co.* v. *Commissioner,* 9 T. C. 183 (1947). The Commissioner of Internal Revenue expressed his agreement with the interpretation of the provisions relating to the taxation of nonresidents involved in these cases by publishing his acquiescence in the *Kimble* case in 1947.

The Internal Revenue Code has been amended a number of times since the decision in these cases, but Congress has indicated no disagreement with them. In the Revenue Act of 1950 the income from copyrights was made taxable to the author in all cases as ordinary income,* whereas the taxability to inventors of the income from patents was deliberately left unchanged. At the same time the exemption of nonresident aliens from capital gain which had been in effect since 1936 was withdrawn in the case of those "temporarily present in the United States."** Had Congress not

---

* §117(a)(1)(C), added by §210(a) of the Revenue Act of 1950.

** §211(a)(1)(B), added by §213(a) of the Revenue Act of 1950.

approved of the *Celanese, General Aniline* and *Kimble Glass* cases, it certainly would have spoken at the same time these two closely related changes were made.

The *Wodehouse* case is thus not only distinguishable on its facts from the instant case, but the principle which it announced leads to the contrary result in the instant case.

RESPONDENT'S THIRD POINT.

"* * * The Decision of the Court Below Is * * * Also Supported By the Decision of the Court of Appeals for the Second Circuit in *Bloch* v. *United States* * * *" (Br. 8).

The *Bloch* case is likewise distinguishable on its facts from the instant case. There the nonresident alien retained incidents of ownership in the patent, including a power of veto over infringement actions.

In the instant case the taxpayer transferred its entire interest, reserving no rights whatever in the patent except security rights to assure the payment of the agreed purchase price.

RESPONDENT'S FOURTH POINT.

"* * * The Effect of This Court's Holding in That Case [*Wodehouse*] Is That Congress Intended That No Agreement Which Purports to Be a Licensing Agreement With Respect to Copyrights and Patents Shall be Treated as a Sale * * * So Long as the Income Taxes Thereon Can Be Easily and Readily Withheld * * *" (Br. 9).

This is a broad and unjustified extension of the holding in the *Wodehouse* case. This Court decided only that the Treasury had asserted its power to withhold tax from the proceeds of the transfer of a *part* of a *copyright* prior

to the enactment of the 1936 Revenue Act and that it was the intention of Congress in enacting that Act to continue to tax all amounts which had theretofore been subject to withholding.

This Court explained the reason for the change in the 1936 Act on the ground that it had been difficult for United States tax officials to ascertain the taxable income (in the nature of capital gains) which had been derived from sales of property at a profit by nonresident alien individuals or by foreign corporations when the respective taxpayers were not engaged in trade or business within the United States. This difficulty was in contrast to the ease of computing and collecting a tax from certain other kinds of income, such as interest and wages, which have no cost basis and therefore consist *wholly of income.* The opinion made it clear that the payments in the *Wodehouse* case were subject to tax because they consisted *"wholly of income * * * in contrast to gains, profits and income * * * from * * * sales of real or personal property"* (pp. 393-394).

"Royalties" which are in fact installments of purchase price, have a cost basis and are not *"wholly income"*. If such installment payments are held subject to withholding, a nonresident alien such as petitioner will be taxed on his gross income and will not be permitted to recover his capital cost.

RESPONDENT'S FIFTH POINT.

"* * * The Payments Received By the Taxpayer * * * Were Payments Which the Parties to the Agreements Themselves Treated as Royalties * * *" (Br. 10).

The taxpayer consistently contended that the "royalties" were in fact installments of purchase price. The fact that the nomenclature of license and royalty were

used is of no significance where the intent is to transfer the beneficial interest in the patent—it is the real substance of the transactions which governs.*

How the transferee treated the payments in the instant case is immaterial. The fact is, however, that the transferee sought a ruling that no withholding was required from the payments on the ground that they constituted installments of purchase price (R. 32, 66).

The Brief for the Respondent Has Attempted to Answer None of the Taxpayer's Arguments.

The decision is clearly erroneous on the following grounds:

(1) It is in conflict with numerous decisions, including decisions of this Court, the Courts of Appeals and the Tax Court (Pet. 5, 14-18).

(2) It erred in holding as a matter of law that the exclusive License Agreement was not a sale of the patents (Pet. 6, 14-18).

(3) It misinterpreted the purpose and legal effect of the Option Agreement (Pet. 18-21).

(4) Despite express provisions in the Agreements to the contrary, it falsely assumed (R. 72) that the licensees could not sue for infringement in their own names (R. 11, 24, 60-61; Pet. 21-23).

(5) It completely ignored Mr. Garrard Winston's sworn statement, which was the only direct evidence as to the intent of the parties (R. 48; Pet. 23-24).

(6) It drew other unjustified inferences from the form of the License Agreement and the related documents (Pet. 25-28).

---

* *Waterman* v. *Mackenzie*, *supra*, and cases cited at pages 16-18 of petitioner's main brief.

Conclusion.

Respondent's brief does not attempt to support the reasoning of the decision of the majority below. It seeks instead to support the result by reliance upon the decision of this Court in the *Wodehouse* case and upon the decision of the Court of Appeals for the Second Circuit in the *Bloch* case, both of which are clearly distinguishable on their facts.

WHEREFORE, for the reasons relied upon in the petition, and for the further reason that respondent contends that the decision of this Court in *Wodehouse* v. *Commissioner,* involving the transfer of a *part* of a *copyright,* is controlling in the instant case, involving the transfer of the *whole* of *a patent,* your petitioner respectfully prays that this petition for a writ of certiorari be granted in order to clarify these important questions of Federal income tax law and to prevent confusion and unnecessary litigation.

Respectfully submitted,

WILLIAM A. PATTY,
Counsel for Petitioner,
20 Exchange Place,
New York 5, New York.

SHARON CLAY RISK,
Of Counsel.